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IN THE

Supreme Court of the United States

OCTOBER TERM 1954

No. 209

KEITH M. BEATY, *Petitioner*,

v.

UNITED STATES OF AMERICA, *Respondent*.

On Petition For a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

SUPPLEMENTAL BRIEF FOR PETITIONER

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SUPPLEMENTAL BRIEF FOR PETITIONER

This supplemental brief is respectfully presented to this Honorable Court for the reason that since the filing of the petition for a writ of certiorari herein and on December 6, 1954, this Court decided the following cases involving the expenditures and/or net worth method of computing income which have an important bearing on Reason II (pages 12-16, inclusive of petition) for the granting of certiorari in this cause: *Holland v. The United States*, Case No. 37; *Friedberg v. The United States*, Case No. 18, and *Smith v. United States*, Case No. 52.

It is respectfully submitted that the dangers or pitfalls in the expenditures or net worth method of computing

income which were pointed out by this Court in these cases are present in this case.

This Court emphasized the importance of the assets on hand at the beginning point of an expenditures-net worth computation but developed with certainty the inherent weakness of the taxpayers' contentions that they had on hand at the crucial beginning point large sums of cash which accounted for the expenditures made during the taxable years involved.

However, in the Beaty case, the cash on hand at the crucial beginning point was proved by the Government itself and the fact that no credit was given the taxpayer for the cash on hand at the beginning of the period in the revenue agent's charts or computations was admitted by Government witnesses themselves. Here is a case where the Government proves the amount of cash on hand at the crucial beginning point and then admits there was no credit given for this cash in the expenditures computations for the taxable years shown on the Government charts. The cash on hand at the beginning of the period was totally disregarded by the United States and its witnesses contrary to the principles enunciated by this Court in *Holland* and *Friedberg*, supra.

In the Beaty case the Government evidence attempting to show additional income in the hands of the petitioner (according to the Government's own expert's admission) was based on items of expenditures in excess of income (R. II, 152).

Government witness Cline, a special agent, testified that he had not given petitioner any credit in his computations for cash on hand as of the beginning of the period, January 1, 1945 (R. I, 136).

Government witness Parrish, a special agent, also testified that he had not given petitioner any credit for

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funds on hand at the beginning of the period (R. I, 153-155).

The Government's own witnesses, bankers, testified that petitioner had on hand at the beginning of the period, January 1, 1945, approximately $100,000 (R. I, 125). Seventy thousand dollars of this money was released to petitioner by the bank on March 20, 1945 (R. I, 129).

Can this defendant, under the decisions of this Court in *Holland, Friedberg* and *Smith,* supra, be convicted on the expenditures basis by disregarding the known cash on hand at the crucial beginning of the period?

This question was answered by this Court in *Smith v. United States of America,* No. 52, 75 S. Ct. 194 at page 198, as follows:

> "• • • Without proof that assets on hand at the beginning of the prosecution period did not account for the alleged net worth increases, the Government could not succeed. Holland v. United States, 348 U.S. 75, 75 S. Ct. 127. • • •"

Mr. Justice Clark, speaking for the Court in the *Holland* case, pointed out that the failure of the Government to run down leads might jeopardize the position of the taxpayer. The Court in this instance was speaking of leads that point back to old transactions and far removed from the prosecution period. In the *Beaty* case the Government was not confronted with the proposition of investigating various and devious leads. But, on the contrary, a simple investigation at the bank would have determined the amount of cash on hand at the beginning of the period, as shown by the bankers at the trial of this case. In the *Friedberg* case the agent testified that there was no evidence available to show that there was cash. In the *Holland* case the admission of the taxpayer, in addition to the factual evidence, did not justify the con-

tention of the cash on hand at the beginning period. In the instant case, the amount of cash on hand at the crucial beginning point was clearly shown, as was the fact that the Government did not give any credit for the known cash at the beginning of the period. The Court below, in its opinion, merely disposed of this point by stating that no explanation was given by the defendant as to the cash on hand at the beginning of 1945. (Petition for certiorari, page 40).

It is respectfully submitted that the petitioner was not called upon to explain the accumulation of assets prior to the years involved and that under the *Holland* and *Friedberg* decisions of this Court, it was reversible error for the Court below to disregard the undisputed evidence of the cash on hand at the beginning of the period and demand from the defendant an explanation of this cash accumulation.

As pointed out by Mr. Justice Clark in the *Holland* case: "Were the taxpayer compelled to come forward with evidence he might risk lending support to the Government's case by showing loose business methods or losing the jury through his apparent evasiveness." The Court further stated that this danger must be minimized.

The explanation of the *Beaty* case is simple. The Government sought to place taxable income in Beaty's, the individual's, hands by showing that in 1945 he spent $32,855.60 more than he reported and $56,595.67 more than he reported in 1946. They, the Agents Cline and Parrish, stated that they had given Mr. Beaty no credit for the cash on hand at the beginning of the period, amounting to approximately $100,000 as shown by the testimony of their own witnesses (R. 125, Vol. I, R. 136, Vol. 1, R. 153-155, Vol. 1).

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It is respectfully submitted that under the *Holland* and *Friedberg* decisions of this Court it was reversible error to allow an expenditure computation to stand without giving full credit for the cash on hand at the crucial beginning point of the computation.

In *Holland v. United States*, supra, Mr. Justice Clark, in speaking for this Court, declared:

* * * *

"As we have said, the method requires assumptions, among which is the equation of unexplained increases in net worth with unreported taxable income. Obviously such an assumption has many weaknesses. It may be that gifts, inheritances, loans and the like account for the newly acquired wealth. There is great danger that the jury may assume that once the Government has established the figures in its net worth computations, the crime of tax evasion automatically follows. The possibility of this increases where the jury, without guarding instructions, is allowed to take into the jury room the various charts summarizing the computations; bare figures have a way of acquiring an existence of their own, independent of the evidence which gave rise to them.

* * * *

"While we cannot say that these pitfalls inherent in the net worth method foreclose its use, they do require the exercise of great care and restraint. The complexity of the problem is such that it cannot be met merely by the application of general rules. Cf. Universal Camera Corp. v. Labor Board, 340 U.S. 474, 489. Trial courts should approach these cases in the full realization that the taxpayer may be ensnared in a system which, though difficult for the prosecution to utilize, is equally hard for the defendant to refute. *Charges should be especially clear, including, in addition to the formal instructions, a summary of the nature of the net worth method*, the assumptions on which it rests, and the inferences available both for and against the accused. *Appel-*

late courts should review the cases bearing constantly in mind the difficulties that arise when circumstantial evidence as to guilt is the chief weapon of a method that is itself only an approximation." (Emphasis supplied.)

• • • •

In the *Beaty* case, the District Court permitted the Government to put before the jury computations illustrated by large placards or charts, which were prepared long before the trial and which purported to show expenditures of approximately $89,000 by petitioner in excess of petitioner's income for the years in question, though Government agents later admitted that they had not given any credit in their computations for the cash the agents knew petitioner had on hand or available as of the beginning of the period for which petitioner was prosecuted. These charts were allowed to remain before the jury throughout the trial; the Government witnesses Parrish and Cline were allowed to testify from the charts; and the jury was continually given the full impact of the charts even though the Government's evidence utterly failed to support and verify the figures on the charts. Truly these charts and figures had "a way of acquiring an existence of their own, independent of the evidence which gave rise to them".

Moreover, the jury was permitted to take these charts that were made up before the trial, and admittedly not based on the evidence, into the Jury Room for perusal and study.

The Court below, in commenting on this particular phase of the trial, stated: (Page 39, Appendix, attached to petitioner's petition) "It does not appear that the charts were formally introduced in evidence, but to all intents and purpose they formed a part of the testimony."

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This is exactly what petitioner complains of, that the jury received the full force and impact of the charts when they were not introduced in evidence and were not substantiated by the Government's testimony and, yet, they were allowed to assume that the figures thereon were true and correct.

The Court of Appeals, in commenting further on this particular phase, said (Page 39, Appendix, attached to petitioner's petition) "Doubtless the more regular procedure would have required the introduction of the supporting evidence before the conclusions of the experts were shown, but this evidence was finally made available and most of it was produced before the cross-examination of the witness began." It is respectfully urged that the Court below was confused and in error to make such a statement, as the majority of the Government's testimony utterly failed to support the conclusions of the experts, but nevertheless the jury was allowed and permitted to get the full impact of the experts' conclusions which overshadowed and rendered insignicant the Government's evidence to the contrary, which later followed.

The Court of Appeals sanctioned the act of permitting the jury to take with them the charts into the jury room on the ground that the attorney for the defendant consented "to putting any and all of the evidence in". (Page 39, Appendix to petition.) This appears to be a self-contradiction, especially in view of the statement of the Court below at the beginning of this paragraph when it said: "It does not appear that the charts were formally introduced in evidence." The statement of defense attorney in nowise consented or agreed to the charts or any other figures or documents which were not evidence (R. 534, Vol. II).

The Government's case against the petitioner was apparently built up on the theory that the Beaty Service

Company, Inc., a corporation, of which petitioner was President and principal owner, earned more money than reported driving cabs during the years in question and that this money was paid to or obtained by the petitioner or defendant below.

The Government experts based their conclusion on a number of assumptions:

(1) That all moneys paid to any agent of the corporation, whether accounted for or not, went into the defendant's hands (R. 340) and the whole sum was taxable as earnings of the defendant (R. 151), and that the same sum was taxable in full as earnings of the corporation (R. 151).

(2) Although the cabs being operated by the company were, on the average, three and one-half years old, that they were operated 100% of the time (R. 177); this in the face of the Government's own evidence that considerably more than $50,000.00 had been paid out for repairs during the same period.

While the Government produced seventy-eight cab drivers and station employees, not one of them testified that the cabs were in continuous operation. To the contrary, more than 90% of them testified that a large percent of the cabs were continuously out of operation and most of them admitted that the moneys due the corporation for the cab rentals were not fully paid.

Contrary to the decisions of this Court in *Holland* and *Friedberg*, supra, the charts were taken into the jury room without guarded instructions. Instead, the instructions given by the trial court were highly prejudicial to the defendant. The charge contained such language as (R. 505, Vol. II):

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"The Government says, Gentlemen of the Jury, among the many bits of evidence from which these contentions might arise, that Mr. Beaty is guilty. It says and contends that he began here in Charlotte, and through determination and perseverance and a certain amount of luck, as we Americans are lucky individuals, that he has made some money, and that after he begun to make money in appreciable amounts that the cost of World War II was such that the rates were obviously compelled to be raised and raised appreciably, and that as those things developed the more man made and in the bigger brackets that he became or the higher altitudes he attained financially that the greater the tax began to be, and that after Mr. Beaty had begun to assume an income in fairly good-sized proportions the Government says that he then began to appreciate the fact that he had best devote some of his efforts toward eliminating some of the income which he had or taking care of it to the extent that he would not be compelled to report it."

Such instructions and procedure by the trial court were distinctly contrary to the principles enunciated by this Court in *Holland v. United States,* supra.

Furthermore, the trial court not only permitted the Government accountants to draw conclusions contrary to the evidence, but also in its rulings on the evidence shifted by direct language the burden of proof from the plaintiff to the defendant. The Court ruled that a Government expert did not need to inquire into the whole case and placed the burden on the defendant to prove the deficiencies in the Government agents' investigations and inquiries. The trial court even foreclosed the defendant's attorney from inquiry on cross-examination as to the extent of the investigation made by the Government agent, the following excerpts from the record being illustrative of this point:

"THE COURT: An expert only knows what he knows. He does not know what he ought to know. Mr. Muskoff, nobody has the foresight of God Almighty. All in the word this man could know would be the papers he examined, and he is only reposible for that. If it should be shown by something he knows that he is in error the Government is bound by that.

"MR. MUSKOFF: Are we bound only to show that he knows?

"THE COURT: How could he testify to that unless he knows, and tell the truth?

"MR. MUSKOFF: Just like your Honor so aptly stated at the closing on Friday, that in this Honorable State no one ever accuses the other unless he is sure he is right. Now what I am trying to demonstrate is that he wasn't sure he was right. * * *"

"THE COURT: He can only know that by what he saw. Now if you have records that he ought to have seen and did not see, then if you can get those records in evidence, they can go to the jury for what they are worth." (R. II, 315).

Again on cross-examination, the witness was being interrogated with reference to the large expenditures that Beaty Service Company paid for wrecker service, the expert witness, Parrish, was asked:

"Did you know that the books of Beaty Service Company showed large amounts of money having been paid to them during the course of the years 1945, 1946 and 1947?

"MR. BEAL: Objection, Your Honor. His tax return shows it, and the Government says it gave him credit.

"THE COURT: Sustained: He says he has no knowledge of it being in the shop, so he could have done otherwise than to charge it up as being in operation.

"Q. As an expert, could you not have looked and ascertained from those bills in the files that these cars could not have been in operation when they were in the shop?

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"A Those records would not give me how long they were in the shop if I had them.

"Q Would not the Pettit Motor Company records have thrown some light on that?

"A Not necessarily as to the length of time they were in there.

"Q Not worthy of being looked into by an expert?

"A I don't believe their records would show that information, sir.

"Q Don't you know as a matter of fact, as an expert, that when you take your car into a well run garage they make out a repair ticket and date it? And then bill it as of the date the repair is finished?

"MR. MONTEITH: If your Honor pleases, we object on the ground that he is not an expert in repair, car repair.

"THE COURT: Objection is sustained because he says he charged up the full amount. If there is subsequent evidence indicating in a positive way that that car was not operating at the then, of course, it would be an error. I do not see how he could know that." (R. II, 275-276).

This is contrary to the rule established in *Holland v. United States*, supra, in which this Court, speaking through Mr. Justice Clark, stated that the burden of proof remains with the Government and does not shift to the defendant and further that if the taxpayer were compelled to come forward with evidence he might risk lending support to the Government's case.

This brief has been devoted to the applicability of the *Holland, Friedberg* and *Smith* decisions of this Court to Reason II (page 12 of petition) for the granting of the petition for certiorari.

Petitioner also relies on the grounds set forth in Reasons I, III, V, VI and VII of the petition. Reason IV has been eliminated by the decision of this Court on December 6, 1954 in *Sullivan v. United States*, Case No. 64.

CONCLUSION

Petitioner respectfully submits that this Honorable Court should grant the petition for certiorari.

Respectfully submitted,

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